

Message Text

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ACTION NEA-09

INFO OCT-01 ISO-00 AID-05 CIAE-00 COME-00 EB-07 FRB-03

INR-07 NSAE-00 TRSE-00 XMB-02 OPIC-03 SP-02 CIEP-01

LAB-04 SIL-01 OMB-01 NSC-05 SS-15 STR-04 CEA-01 L-02

H-02 DODE-00 PA-01 USIA-06 PRS-01 IO-10 AGR-05 /098 W
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TO SECSTATE WASHDC 6374

INFO AMEMBASSY NEW DELHI

AMCONSUL CALCUTTA

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E.O. 11652: N/A

TAGS: EFIN, BG

SUBJECT: DEMONETIZATION

REF: DACCA 1703

1. THREE-DAY PERIOD FOR DEPOSITING DEMONETIZED ONE-HUNDRED TAKA NOTES ENDED APRIL 9 WITH TOTAL COLLECTIONS ESTIMATED AT ROUGHLY ONE-HALF OF TOTAL OUTSTANDING SUCH NOTES. BDG ANNOUNCED APRIL 9 THAT QTE TO MINIMIZE THE DIFFICULTIES OF THE SMALL INCOME PEOPLE, THE GOVERNMENT HAVE, FOR THE TIME BEING, DECIDED THAT THOSE WHO DEPOSITED UP TO TAKA 500 MAY DRAW UP TO TAKA 300 FROM APRIL 12...THE PROCEDURE OF RETURN OF THE REMAINING DEPOSITED AMOUNTS WILL BE ANNOUNCED LATER END QTE. (TEXT PRESS NOTE FOLLOWS BY AIRGRAM.)

2. TOTAL MONEY SUPPLY (NARROWLY DEFINED) WAS SLIGHTLY OVER 9 BILLION TAKA OF WHICH DEMAND DEPOSITS TOTALLED 5 BILLION AND NOTES 4 BILLION. ONE-HUNDRED TAKA NOTES TOTALLED ABOUT 1.85 BILLION WITH ABOUT 20 BILLION HELD
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IN COMMERCIAL BANKS. OF REMAINING 1.65 BILLION WITH

PUBLIC, SOME 800 TO 850 MILLION WORTH OF ONE-HUNDRED TAKA NOTES WERE ACTUALLY DEPOSITED. (RETURNS ARE STILL COMING IN FROM RURAL BANK BRANCHES--WE EXPECT HAVE MORE PRECISE FIGURES LATER.) INFORMATION FROM ONE FOREIGN BANK SUGGESTS AVERAGE OF OVER 2000 TAKA PER DEPOSITOR.

3. BANGLADESH BANK ECONOMIC ADVISER ESTIMATED THAT 20 PERCENT OF 100-TAKA NOTES IN CIRCULATION WERE OUTSIDE BANGLADESH (LARGELY IN INDIA) AND AN ADDITIONAL 20 PERCENT IN RURAL AREAS AND WERE NOT RPT NOT TENDERED AT BANKS. (ONE FACTOR IN RURAL AREAS WOULD BE VILLAGERS' DISTRUST OF BDG CIVIL SERVANTS GENERALLY, INCLUDING BANKERS, WHO ENJOY REPUTATION OF EXTORTING PRICE FOR RENDERING SERVICES SUCH AS ACCEPTING DEPOSITS FROM ILL-INFORMED OR CONFUSED RURAL FOLK.)

4. BDG CLOSED LAND AND SEA BORDERS FROM THE APRIL 6 ANNOUNCEMENT THROUGH APRIL 9 AND CHECKED ALL ARRIVING AIR PASSENGERS, ESPECIALLY FROM INDIA, TO LIMIT INFLOW OF NOTES FROM ABROAD.

5. POLITICIANS HAVE HAILED DEMONETIZATION AS ANTI-CORRUPTION AND ANTI-INFLATION MOVE. NEWSPAPERS QUOTED ONE BAKSAL MEMBER AS SAYING QTE THIS STEP OF...PRESIDENT MUJIBUR RAHMAN WOULD INFLICT A CRUSHING BLOW ON THE SMUGGLERS, PROFITEERS, HOARDERS, CORRUPT ELEMENTS AND HIJACKERS (SIC) ON THE ONE HAND, AND CURB INFLATION AND ARREST PRICE SPIRAL ON THE OTHER END QTE.

6. IMMEDIATE EFFECT OF DEMONETIZATION HAS, THUS, BEEN TO REDUCE MONEY SUPPLY BY ABOUT 20 PERCENT, BUT IN ABSENCE ANY FURTHER INFORMATION ON DISTRIBUTION OF NOTES, VELOCITY OF MONEY, OR SPEED WITH WHICH GOVERNMENT WILL REIMBURSE DEPOSITORS, IT DIFFICULT JUDGE ANTI-INFLATION EFFECT. (RETAIL PRICES OF SOME BASIC COMMODITIES, INCLUDING RICE, IN DACCA WERE SOMEWHAT LOWER APRIL 9 AND 10 THAN APRIL 12; NO SUCH COMMODITIES' PRICES ROSE.)

7. OUR FIRST IMPRESSIONS ARE:

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(A) ANNOUNCEMENT WAS, IN FACT, SURPRISE. WHILE IDEA HAD BEEN CONTEMPLATED, AND HENCE BEEN SUBJECT OF RUMORS FOR PAST YEAR, DECISION TAKEN ONLY EVENING OF APRIL 4 (AT HIGH-LEVEL MEETING WITH PRESIDENT, WHICH SPARKED INEVITABLE RUMOR OF DEVALUATION), AND TIMING UNKNOWN IN ADVANCE. FOREIGN BANKER TOLD EMBOFF HE HAD HAD NO ADVANCE INFORMATION OR HINT WHATSOEVER. STORY IS THAT IN INFORMING FELLOW MINISTERS AT 8:30 P.M.

APRIL 6, FINANCE MINISTER HELD THEM IN HIS OFFICE
UNTIL 9 P.M. ANNOUNCEMENT MADE.

(B) OUTCOME. OPERATION WAS TECHNICAL SUCCESS.
DEPOSIT PROCESS WENT SMOOTHLY, AND LARGE PORTION OF
NOTES OUTSTANDING WERE NOT DEPOSITED.

(C) BLACK MONEY. IT IS NOT SO CLEAR WHO LOST BY
THIS OPERATION. WE DOUBT ANY SIGNIFICANT PORTION OF
FUNDS ABROAD WERE RETURNED. (IT IS ILLEGAL TAKE TAKA
ABROAD.) TO THAT EXTENT, BLACK MONEY-HOLDERS WERE
CAUGHT. IN BANGLADESH, THERE WAS CONSIDERABLE SCRAMBLE
AND, AGAIN A FIRST IMPRESSION, WE THINK NUMEROUS HOLDERS
OF ILLEGAL FUNDS WERE ALSO CAUGHT. BUT THE BIGGEST
FISH, WHO HOLD FUNDS ABROAD, HAVE INVESTED IN REAL
ESTATE, ETC., CAN HARDLY HAVE BEEN MORE THAN INCONVENIENCED,
AND, OF COURSE, DEMONETIZATION DOES NOT RPT NOT REMOVE
ROOT CAUSES OF CORRUPTION.

(D) ANTI-INFLATION. AS INDICATED ABOVE, WE ARE
NOT SURE OF DEGREE TO WHICH DEMONETIZATION MAY PROVE
ANTI-INFLATIONARY, BUT AS BANGLADESH BANK GOVERNOR
NOTED TO EMBOFF, ANY REASONABLE DEGREE OF SUCCESS IN
REDUCING AMOUNTS OF BALCK MONEY WOULD ITSELF HAVE SOME
ANTI-INFLATIONARY EFFECT.

(E) POPULAR MOVE. THIS GOVERNMENT ACTION, AIMED
AT BLACK MONEY, SMOOTHLY EXECUTED AND CATCHING FUNDS
HELD BY INDIANS APPEARS TO BE POPULAR WITH MANY
BANGALEES.

(F) COMMERCIAL EFFECT. DEMONETIZATION HAS DISRUPTED
COMMERCIAL ACTIVITY, WITH LARGER FIRMS LEGALLY REQUIRED
TO MEET MONTHLY PAYROLLS BY 10TH OF MONTH ESPECIALLY
INCONVENIENCED. RAPID REPLACEMENT OF DEPOSITED FUNDS
WOULD GREATLY EASE SITUATION.

(G) NEXT STEPS. WE DO NOT KNOW WHAT BDG INTENDS
TO DO NEXT, BUT IT WIDELY SUPPOSED HERE THAT LARGER
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DEPOSITS WILL BE EXAMINED AND DEPOSITORS' FUNDS REPLACED
GRADUALLY. FOREIGN BANKERS TELL US THEY HAVE NO RPT
NO NEW TAKA NOTES IN VAULTS AWAITING ISSUE, BUT WE
UNAWARE WHETHER BANGLADESH BANK HOLDING NEW TAKA NOTES
OR NOT. (THERE IS REPORT THAT SHIPMENT OF NEW BANK
NOTES ARRIVED CHITTAGONG A MONTH AGO.)

(H) SEVERAL OBSERVERS DOUBT BDG OFFICIALS HAVE
THOUGHT ENTIRE OPERATION THROUGH TO CONCLUSION AND
THAT FAILURE REPLACE NOTES PROMPTLY WILL SERIOUSLY
DISRUPT COMMERCIAL ACTIVITY. OUR VIEW, HOWEVER, IS
THAT UP TO THIS POINT AT LEAST, OPERATION HAS GONE
WELL. IF IT CONTINUES TO BE CONDUCTED EQUALLY WELL IN
FUTURE, IT WILL BE FIRST ECONOMIC MEASURE SINCE SECOND
REVOLUTION TO MERIT OUR RESPECT. SO FAR, IT CONTRASTS
SHARPLY WITH, SAY, JUTE POLICY ANNOUNCEMENT. CREDIT

FOR THIS MOVE MUST GO TO BANGLADESH BANK GOVERNOR
WHO ALSO INSTITUTIONALIZED AS PART OF REGULAR BUDGET
OPERATIONS THE JUTE MILL SUBSIDIES IN JANUARY, AND IS
EMERGING AS A KEY BDG ECONOMIC POLICY-MAKER.
BOSTER

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